

Early Sunset of the Employee Retention Credit

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The Employee Retention Credit (ERC) was designed to help employers retain employees during the Coronavirus Disease 2019 (COVID-19) public health emergency. The Infrastructure Investment and Jobs Act (IIJA, P.L. 117-58) moved the termination date for the credit forward, to September 30, 2021, from December 31, 2021. This change effectively repeals the ERC for the fourth quarter of 2021 for businesses other than recovery startup businesses. Some employers may have anticipated receiving the ERC for the fourth quarter (the IIJA was signed into law on November 15, 2021), and therefore either underpaid their employment tax liability or received an advance refund from the IRS. IRS [guidance](#) provides that taxpayers who received ERC advance payments in the fourth quarter of 2021 must repay those amounts. The IRS also provided relief from late deposit penalties for employers that reduced payroll tax deposits in anticipation of receiving the ERC in the fourth quarter of 2021.

Employee Retention Credit: Summary and Legislative History

The credit was first enacted in the [Coronavirus Aid, Relief, and Economic Security Act](#) (CARES Act, P.L. 116-136) in March 2020. The ERC allowed businesses to claim a refundable credit against their payroll tax liability for a percentage of wages they paid to workers after March 12, 2020, and before January 1, 2021. Initially, the credit was 50% of up to \$10,000 in qualifying wages. Eligible employers included those who (1) were required to fully or partially suspend operations due to a COVID-19-related order (including nonprofit employers); or (2) had gross receipts 50% less than gross receipts in the same quarter in the prior calendar year (with the credit no longer available once gross receipts were 80% of prior year calendar quarter gross receipts). Eligible employers included tax-exempt organizations. Employers with more than 100 full-time employees could only claim the credit for wages paid when employee services were not provided. Employers with 100 or fewer full-time employees could claim the credit for any otherwise qualifying wages that were paid.

The credit was structured so that employers could be reimbursed when processing payroll by reducing required deposits of payroll taxes by the anticipated amount of the credit. Many businesses make regular payroll tax payments with their payroll cycle (e.g., biweekly). The credit was also advanceable, meaning

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that businesses expecting credit amounts in excess of payroll tax liability could file for an advance payment from the IRS. These reductions in payroll taxes paid and advance payments were then reconciled with the business's actual payroll tax liability and ERC amount on quarterly payroll tax filings with the IRS.

The [ERC was subsequently extended by the Taxpayer Certainty and Disaster Tax Relief Act of 2020](#) (Division EE of the Consolidated Appropriations Act, 2021, P.L. 116-260), which applied to wages paid from January 1, 2021, through June 30, 2021. P.L. 116-260 increased the maximum credit available from \$5,000 (50% of \$10,000 in qualifying wages) to \$14,000 (70% of \$20,000 in qualifying wages). The legislation modified the eligibility such that employers that had gross receipts 20% less than gross receipts in the same quarter in the prior calendar year or prior calendar quarter could qualify. The threshold below which employers could claim the credit for all wages paid, as opposed to claiming it for wages paid only when services were not provided, was increased to 500 full-time employees.

The ERC Before the IIJA Modification

The most recent ERC extension was in the [American Rescue Plan Act of 2021](#) (ARPA, P.L. 117-2). When ARPA became law in March 2021, the ARPA ERC applied to wages paid between July 1, 2021, and December 31, 2021. Under ARPA, a credit of 70% on up to \$10,000 in wages was allowed for the third and fourth quarters of 2021. Thus, under ARPA, the maximum credit amount for 2021 was increased from \$14,000 to \$28,000 (or \$7,000 per quarter for the full 2021 calendar year). A credit of up to \$50,000 per calendar quarter was also provided to *recovery startup businesses*, defined as businesses established after February 15, 2020, with average annual gross receipts that do not exceed \$1 million. Severely financially distressed employers, those with gross receipts that were less than 10% of what they were in the same calendar quarter in 2019, were able to treat all wages as qualifying wages.

Early Sunset in the Infrastructure Investment and Jobs Act

The Infrastructure Investment and Jobs Act (IIJA, P.L. 117-58), signed into law by President Biden on November 15, 2021, changed the dates of the ARPA ERC extension. Specifically, the IIJA changes the ERC to apply to wages paid between July 1, 2021, and September 30, 2021 (unless the wages are paid by an employer that is a recovery startup business).

The IIJA passed the Senate on August 10, 2021. At that time, the proposed change to the ERC would have been a future change, rather than a retroactive one. However, the House passed the Senate version of the act on November 5, 2021, and it was signed into law by President Biden on November 15, 2021. This caused what would have been a prospective change in tax law to be a retroactive change in tax law. Because the retroactive repeal of the ERC did not occur until mid-November, some employers may have already taken action regarding fourth quarter employment taxes with the expectation that the ERC would still be available.

What Can Businesses Do?

The IRS released [guidance](#) for businesses other than recovery startup businesses that anticipated receiving the ERC for the fourth quarter. Employers that requested and received an advance refund of the ERC for the fourth quarter must repay the amount by the normal due date of their employment tax return (for many employers, this will be January 31, 2022).

Other employers may have reduced their regular payroll deposits during the quarter by the amount they expected to receive from the ERC. The IRS will waive failure to pay penalties for employers who anticipated receiving the ERC between October 1, 2021, and December 20, 2021, if the employer

1. Reduced deposits accurately for the expected ERC amount,
2. Deposits the amounts initially retained by the normal due date (for many employers, this will be January 31, 2022), and
3. Reports the tax liability due on the full amount of wages paid during regular filing.

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